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No. 458

IN THE

Supreme Court of the United States

OCTOBER TERM, 1965

BEN POLIKOFF,

Petitioner,

vs.

MAURICE S. LEVY, LOUIS C. RAPPAPORT, HARRY MILLER and SIDNEY MILLER,

Respondents.

On Petition for a Writ of Certiorari to the Appellate Court of Illinois First District

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BRIEF FOR THE RESPONDENTS IN OPPOSITION

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On Petition for a Writ of Certiorari to the Appellate Court of Illinois First District

BRIEF FOR THE RESPONDENTS IN OPPOSITION

To The Honorable Chief Justice and Associate Justices of The Supreme Court of The United States:

Respondents, Maurice S. Levy, Louis C. Rappaport, Harry Miller and Sidney Miller, submit this Brief in opposition to the Petition for Writ of Certiorari.

Respondents assert that the Petition presents no ground which justifies the issues of a Writ.

There are no conflicting decisions rendered by any State or Federal Courts of Appeals on the principles of law decided in the instant case by the Appellate Court for the First District of Illinois. The basic question of law decided and followed by the Appellate Court for the First District of Illinois in this case was in accordance with the decision of this Court in *Securities and Exchange Commission* v. *W. J. Howey Co.*, 328 U.S. 293 (1946). This decision does not require clarification or revision in any manner.

I.

QUESTIONS PRESENTED

The two "Questions Presented" at Page 2 of petitioner's Petition do not accurately or correctly reflect the questions of law decided by the Appellate Court of Illinois for the First District in this case.

The recital of facts in the petitioner's Petition for Certiorari is incomplete and insufficient, and the missing facts are supplied shortly in this brief.

The only possible basis for civil liability in this case for an alleged violation of Section 77e (a) and (c) Title 15 U.S.C.A. of the Securities Act of 1933, as amended, would be the use of the mails by the respondent Levy in his dealings with the petitioner Polikoff. Section 77(m) of the Act bars all action for such an alleged violation one year after the alleged violation occurred. This limitation bar is not a personal defense but is a substantive requirement that casts the duty on the complaining party to plead and establish that he filed his action within the statutory period of one year. In the instant case, the plaintiff filed his action long after the one year period. This is amplified later.

The opinion of the Appellate Court of Illinois for the First District and the record of this case establish the following factors:

1. The petitioner, Polikoff, almost at its inception, joined the group that eventually completely paid for the land that was the site of the State House Motor Hotel, and constructed and completed the motel.

2. The petitioner, Polikoff, was a member of a joint venture in this enterprise. He had and exercised an equal right of management and control of the project, and actively participated in its management and control.

3. The petitioner, Polikoff, did not make his payments into the project in reliance on and expect profits solely from the efforts of any third parties.

4. The petitioner, Polikoff, was not an investor. He was a co-owner of real estate, a motor motel.

II.

PLAINTIFF'S FEDERAL ACTION IS BARRED BY LIMITATIONS

As previously stated, the only possible basis for civil liability in this case for an alleged violation of the Securities Act of 1933, as amended, would be the use of the mails by the respondent, Levy, in his dealings with the petitioner, Polikoff. Section 77 (m) of the Securities Act of 1933, as amended, bars all action for such an alleged violation one year after it occurred. Although the certified printed Abstract of Record filed in this case by the petitioner indicates at Page 1 by the memorandum, "Placita of May 1963", that plaintiff's suit was filed in the trial court on May 6, 1963, in fairness to the petitioner and in

the interest of accuracy, we are informing the court that the correct date the complaint was filed in the trial court by the petitioner was November 7, 1962. The last letter written by the respondent, Levy, to the petitioner, Polikoff, after the latter made a payment of $7,500.00 in the project, is dated December 7, 1960. (Abst. 10, 11). Consequently the suit was filed more than a year after the last use of the mails by the respondent, Levy, in the transaction.

The following cases hold that in an action based on a violation of the Securities through the use of the mails, the one year bar of the statute of limitations is not merely procedural, but substantive, and filing suit within the year is an essential ingredient of the cause of action, and that a failure to plead facts in conformity with this limitation section is fatal to claims of this kind.

Here are several of the cases that have decided this settled rule: *Osborne* v. *Mallory,* 86 F. Supp. 869, 873 (1949) (D.C.S.D. N.Y. 1949); *Newberg* v. *American Dryer Corporation,* 195 F.Supp. 345, 352 (1961) (D.C. Pa. 1961); *Premier Industries* v. *Delaware Valley Financial Corporation,* 185 Fed. Supp. 694, 695 (D.C. Pa. 1960).

The remaining points in this brief are set forth without waiving the foregoing limitations complete defense.

III.

THE HOWEY CASE DOES NOT REQUIRE ANY MODIFICATION.

The basic test announced in *S. E. C.* v. *Howey Co.,* 328 U.S. 293, as to whether the transaction is subject to the Federal and State Blue Sky Laws, has been uniformly and consistently followed by the Federal Courts and State Courts.

This test, both within the Federal and State Blue Sky Acts, is a contract, transaction or scheme whereby one person invests his money in a common enterprise on the theory that he expects to receive profits solely from the efforts of others.

The opinion of the Appellate Court of Illinois for the First District in the instant case stressed this test twice in its opinion. It is still an excellent measuring rod. The petitioner in his brief was in error when he stated at Page 10 of his petition that this court has never had occasion to discuss the significance of this test.

In 1959 this Court decided *S. E. C.* v. *Variable Annuity Company,* 359 U.S. 65. The *Howey* decision and this test was discussed by this court at pages 72 and 80 of this opinion.

The test in the *Howey* case was discussed in the following cases decided by various Courts of Appeal: *U. S.* v. *Herr,* 338 Fed. 2d 609 (1964, 7th Cir.); *Roe* v. *U. S.,* 287 Fed. 2d 435, 438 (1961, 5th Cir.); *Roe* v. *U. S.,* 316 Fed. 2d 617, 620 (1963, 5th Cir.); *Moses* v. *Michael,* 292 Fed. 2d 614, 618 (1961, 5th Cir.); *Los Angeles Trust and Mortgage Exchange* v. *S. E. C.,* 264 Fed. 2d 199, 212 (1959, 9th Cir.). The limitations of space prevent the citation of many more Federal cases on this point.

The opinion of the Appellate Court of Illinois for the First District cited *Sire Plan Portfolio, Inc.* v. *Carpentier,* 8 Ill. App. 2d 354, 132 N.E. 2d 78 (1956) and *Meihsner* v. *Runyon,* 23 Ill. App. 2d 446, 163 N.E. 2d 236 (1960). These cases also relied on the *Howey* test.

This *Howey* test was not decided for the first time by this court in its decision in 328 U.S. 293. The opinion itself points out that this test was the basis of many state court decisions. In deciding the *Howey* case, this court followed the applicable principles of state court decisions and it had this comment in its opinion:

> "This definition was uniformly applied by state courts to a variety of situations where individuals were led to invest money in a common enterprise with the expectation that they would earn a profit solely through the efforts of the promoter or of someone other than themselves."

Here are some sample authorities that were based on this same principle before the *Howey* decision was decided by this court. These cases are:

Securities & Exch. Comm. v. *Bailey,* 41 F. Supp. 647 (1941);

Domestic & F. Petroleum Co. v. *Long,* 4 Cal. 2d 547, 51 P. 2d 73 (1935);

Securities & Exch. Comm. v. *Pyne,* 33 F. Supp. 988; 39 F. Supp. 434 (1941);

Prohaska v. *Hemmer-Miller Development Co.,* 256 Ill. App. 331, 336 (1930).

Here again the limitations of space prevent the citation of many more state court decisions on this same point.

This *Howey* test has served well as a guide for the public and the courts and requires neither qualification, modification nor any whittling away of any kind.

IV.

THE FACTS

PETITIONER ACQUIRED AN UNDIVIDED FRACTIONAL INTEREST IN REAL ESTATE, BEING THE LAND AND IMPROVEMENTS OF THE STATE HOUSE MOTOR MOTEL.

The omitted facts in the petitioner's petition now follow. It is necessary to present them so that this court can have a complete picture of the entire transaction.

Count IV of petitioner's amended complaint filed in the trial court is the basis of petitioner's claim in this court. (Abst. 22-25, 50-51). It incorporated by reference the allegations in paragraphs 1, 2, 3, 4, 5, 6, 7, 8 and 9 of Count I (Abst. 22, 1-10). All of the facts that follow are taken from Count IV of petitioner's amended complaint. (Abst. 1-11, 22-26)

The letter-receipts of the respondent, Maurice S. Levy, to the petitioner, Ben Polikoff, which are incorporated in his Amended Complaint, reflect the transaction.

The respondents, Maurice S. Levy, Louis C. Rappaport, Harry Miller and Sidney Miller, initiated the project. When the respondent Levy wrote the November 25, 1959 letter to the petitioner Polikoff (Abst. 2-3), the entire group that finally constituted the members of the joint adventure was far from completed. All of the capital necessary to complete the purchase of the land which became the site of the State House Motor Motel and the funds that would be used to construct the motel on the site with proposed mortgage proceeds had not yet been raised. The respondent Levy's letter of November 25, 1959, to the

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The reference herein to "Abst." is the page number in the printed Abstract of the Record filed by the Petitioner.

petitioner, Polikoff, mentioned that a commitment of a mortgage should "come through any day." The "prospectus or statement" which accompanied the letter mentioned that $665,000.00 was the total capital required, and this statement showed a projection of substantial estimated annual profits. (Abst. 4-5).

In the November 25, 1959 letter from the respondent Levy to the petitioner, Polikoff, Levy wrote "As you know a group consisting of my brothers-in-law, Al Wolf and others have interests in several parcels of real estate in Chicago, and we are going into a new venture. . . . If you are interested please let me know as I am desirous of procuring people in this picture who we know and not go outside our friends." (Abst. 2-3)

Thus, this was not a public offering.

When the respondent Levy in this letter of November 25, 1959, mentioned that "we have purchased a parcel of real estate in Springfield, Illinois . . . " the word "purchased" must be qualified by the allegation in paragraph 2 of Count I of the Amended Complaint that "each of the defendants providing part of the *earnest money* and other *payments* made on *account* of the purchase price thereof." (Emphasis added.) (Abst. 6).

This qualifying language established that when this November 25, 1959 letter was written, all that was paid on account of the purchase of the real estate site for the State House Motor Motel was earnest money and some payments on account on the contract of purchase.

During a period of more than a year *after* November 25, 1959, "40 or more people" paid approximately $500,000.00 into the project (Abst. 7).

The petitioner, Ben Polikoff, made his first payment of $25,000.00 into the project on December 7, 1959. At all times mentioned in the petitioner's Amended Complaint the respondent Levy, with the acquiescence of all other persons who became interested in the project, acted as temporary custodian of the funds for the motel enterprise. After the petitioner Polikoff, made his first payment of $25,000.00, which was acknowledged by the respondent Levy's letter of December 7, 1959 (Abst. 8), more than a year elapsed before the $500,000.00 approximate capital was contributed by 40 or more people (Abst. 7). Moreover, at the time petitioner Polikoff made his first payment of $25,000.00 on December 7, 1959, all the initial group then had was a contract to purchase the land which became the site of the State House Motor Motel. Accordingly, the petitioner Polikoff, was one of the original members of the group that constituted the joint adventure.

In order to demonstrate that the petitioner, Polikoff, purchased a fractional interest in real estate and improvements thereon, we will quote portions of the letters-receipts given by the respondent Levy to the petitioner Polikoff and emphasize the decisive language therein.

The beginning of the December 7, 1959 letter-receipt of the respondent Levy to the petitioner Polikoff mentions receipt of his check for $25,000.00 "for the purpose of acquiring an INTEREST in the contemplated building at the above MOTEL in Springfield, Illinois." (Abst. 8). That letter-receipt concluded with the statement that the letter was a tentative receipt until "the actual agreements and other documents are prepared and delivered to you."

Right after the petitioner's Amended Complaint quoted this letter of December 7, 1959, there is an allegation that the "certificate" representing so-called "units" mentioned

in the letter dated November 25, 1959, were not given or sent to the plaintiff. Nowhere in any of the writings in the petitioner's Amended Complaint was there any actual or implied promise by any of the respondents to give the plaintiff any kind of a certificate. On the contrary, the respondent Levy in his correspondence with the petitioner Polikoff kept referring to AGREEMENTS and other documents that would be delivered to the petitioner.

In the light of the context of all the allegations in the petitioner's Amended Complaint, and viewing the entire transaction in substance as depicted in the petitioner's Amended Complaint, and invoking the cardinal rule of strict construction against the pleader, it must follow that when the respondent Levy stressed agreements and other documents in these letter-receipts, the parties had in mind agreements for either a general partnership, a limited partnership or other similar device where each member of the group would have the right of equal ownership of the property of the venture as well as equal control with the others.

The language "units of $10,000.00 each" by the respondent Levy in his letter-receipt to the petitioner Polikoff was nothing more or less than a convenient method adopted as a standard of computation to determine the fractional interest of each member of the group in the land which was the site of the State House Inn and the Motel itself to be built thereon. Webster's New World Dictionary of the American Language, (1960), defines "unit" in part as, "any fixed quantity, measure, etc. used as a standard."

When the respondent Levy in his letter-receipt of December 7, 1959, advised the petitioner Polikoff that he acquired an "INTEREST" in the contemplated building,

this could have no other meaning than that the petitioner Polikoff acquired a pro-rata fractional interest in the real estate, the site of the State House Motor Motel.

On February 2, 1960, the respondent Levy wrote the petitioner Polikoff another letter in which respondent Levy acknowledged the receipt of another $25,000.00 payment "which represents the balance due for the purpose of acquiring a $50,000.00 'INTEREST' in the contemplated BUILDING of the above motel in Springfield, Illinois." That letter also concluded with the statement that the letter is a tentative trust receipt until "the actual agreements and other documents are delivered to you." (Abst. 9). Here we have a second document which evidences the petitioner's purchase of an additional fractional interest in real estate.

Now we come to the most decisive and illuminating letter-receipt of the entire series. Under date of December 7, 1960, ten months after the previous payment, the respondent Levy wrote the petitioner Polikoff a letter-receipt which acknowledged receipt of Polikoff's check for $7,500.00 representing "*your proportionate share* of the monies necessary for the *purchase of the vacant lot* which will be included in our motel project." (Abst. 10). This lot was to be used as a parking lot in the motel venture (Abst. 21). This letter also concluded that the receipt was "in the form of a tentative trust receipt until the documents are available for signature."

We pause at this moment to emphasize that these letter-receipts of Levy proved conclusively and beyond the shadow of any doubt that the petitioner Polikoff paid for an undivided fractional interest in real estate.

The petitioner, when he prepared his record for the Appellate Court, incorporated the answer of the respondent, Levy, as a part of the record which was filed in the Appellate Court of Illinois for the First District, and later with the Supreme Court of Illinois (Abst. 48). The other respondents adopted Levy's Answer (Abst. 47).

It is important to note that this answer was designated as part of this record by the petitioner.

The petitioner did not abstract the contents of this answer. It is still on file with the Supreme Court of Illinois, and we are filing with this brief a certified copy of this answer. It contains several significant exhibits attached thereto.

Although this case can be and was decided without considering this answer, it is a most revealing document. It blue prints the active and principal participation of the petitioner in the management and operation of the enterprise.

This answer by itself establishes that the petitioner's petition is totally without merit.

Exhibit "B" attached to the answer, is a photocopy of a trust agreement dated June 8, 1961, whereby the legal title to the parking lot in the motel project was placed in trust with the beneficiary being designated as the State House Inn, a limited partnership.

Out of a group of at least 40 persons in the enterprise, four were designated as having the right of direction to deal with the property. They were the respondents, Levy, Rappaport, and Harry Miller, and the petitioner, Ben Polikoff.

Exhibits "C" and "E" attached to the answer is a notice dated November 18, 1960, signed by the respondents, Levy, Rappaport, and Harry Miller, and the petitioner, Polikoff, requesting the members of the project to pay additional funds into the enterprise.

The petitioner was more than just a member of this group of 40 persons. He was one of the leaders and managers of the group and this is evidenced by the exhibits that were just described. What greater participation and right of management can a person have than calling on others in the group to pay more money into the project?

Exhibit "D" attached to the answer, being Articles of Limited Partnership, is dated as of January 1, 1960, signed by practically all of the members of the group, and the respondents, Levy, Rappaport and Harry Miller, together with the petitioner, Polikoff, are designated as the *general* partners.

In addition to his important rights of management and control of the project, the petitioner, Polikoff, paid for and acquired a direct, undivided interest in real estate, as disclosed by the previous exchange of letters between him and the respondent, Levy.

V.

THE SALE OF AN UNDIVIDED INTEREST IN REAL ESTATE IS NOT SUBJECT TO THE SECURITIES ACT OF 1933.

In *State* v. *Golden*, 216 Minn. 97, 12 N.W. 2d 617 (1943), the Supreme Court of Minnesota at page 619 stated:

> "When persons associate themselves together in the purchase of land, they do not come within the provision of the Blue Sky Law."

Unquestionably, the petitioner acquired an undivided interest in real estate and a transaction of this kind is not subject to any Blue Sky Statute, State or Federal.

VI.

IN LINE WITH OTHER STATE COURT DECISIONS, ILLINOIS AUTHORITIES FOLLOW THE GENERAL RULE THAT A SALE OF REAL ESTATE OR A FRACTIONAL INTEREST THEREIN IS NOT SUBJECT TO BLUE SKY STATUTES. BY ANALOGY THIS RULE IS APPLICABLE TO THE SECURITIES ACT OF 1933.

Brothers v. *McMahon*, 351 Ill. App. 321, 115 N.E. 2d 116, was decided in 1953, and held that a receipt-prospectus describing a co-operative housing project similar to the type that was to be purchased, and a standard contract for the construction and purchase of a dwelling unit, including an agreement by the purchaser to agree with other purchasers who would reside in the same dwelling unit of either a corporation or a land trust method of cooperative management of the unit, *was a contract for the sale of real estate* and not a security within the meaning of the Illinois Blue Sky Law. In that case, the court stressed the test we discussed earlier in this brief that to be a Blue Sky instrument the investor must rely on the efforts of others to receive profits.

In *In Re Estate of McCormick*, 284 Ill. App. 543, 1 N.E. 2d 769 (1936), the court also held that an installment real estate contract whereby the vendors agreed to convey title to the vendee upon payment of all installments was held not to constitute the sale of a security under the Illinois Blue Sky Statute.

In *McCormick* v. *Shively*, 267 Ill. App. 99 (1932), the court also held that a contract for the purchase of real estate is not subject to the Illinois Blue Sky Law.

These Illinois decisions which follow other State Court decisions, by analogy are applicable to the Securities Act of 1933.

VII.

THE PETITION FOR CERTIORARI CONCEDES THAT THE ENTERPRISE WAS A JOINT VENTURE, AND THAT MEMBERS OF A JOINT VENTURE WHO POOL THEIR FUNDS AND BUY REAL ESTATE ALSO HAVE THE STATUS OF TENANTS IN COMMON WITH EQUAL RIGHT OF CONTROL AND POSSESSION.

A joint adventure has been defined to be an association of two or more persons to carry out a single enterprise for profit. 23 Illinois Law and Practice "Joint Adventures," Page 59, Sec. 1.

No specific formal agreement is necessary to establish a joint adventure, but the nature of the enterprise undertaken controls. 23 Illinois Law and Practice "Joint Adventures," Page 61, Sec. 2.

In *Ditis* v. *Ahlvin Construction Company,* 408 Ill. 416, 427, 97 N.E.2d 244 (1951), the Supreme Court of Illinois stated:

> "Similar enterprises for the purchase and sale of real estate for profit, which have been reported in the decisions of this court (*Harmon* v. *Martin,* 395 Ill. 595; *Hagerman* v. *Schulte,* 349 Ill. 11), have been held to be joint adventures having, in general, the legal incidents of a partnership, and while it is said that a joint adventure is not regarded as identical with a partnership, the relation of the parties is so similar that their rights and liabilities are usually tested by the rules which govern partnerships. We have further held, in considering such land trading ventures, that the parties engaged in such an enterprise, though no general

partnership exists, are partners in the particular transaction. (*Parish* v. *Bainum*, 306 Ill. 618.) The last-cited case, quoting from *Meehan* v. *Valentine*, 145 U.S. 611, points out that the requisites of a partnership are that 'the parties must have joined together to carry on a trade or adventure for their common benefit, each contributing property or services, and having a community of interest in the profits.' We also pointed out in the *Parish* case that an agreement to share losses is not necessary to constitute one a partner, but that the test is sharing in the profits. Measured by these decisions, the conclusion is strengthened that the substance of the relationship created between the parties by their transactions was that of joint adventurers."

In *Johnson* v. *Farmers & M. State Bank*, 152 Minn. 442, 189 N.W. 583 (1922), the directors of a bank entered into an arrangement whereby each contributed money for the purchase of a farm. Title to the farm was placed in the bank in trust. The proceeds of a sale of the farm were to be divided between the parties in proportion to the amount each contributed. The arrangement was held to be a joint adventure with the parties also being tenants in common.

Since members of a joint adventure who pool their funds and buy real estate also have the status of tenants in common, let us consider the attributes of that relationship which also existed between the petitioner, the respondents and the other members of the State House Motor Motel project.

In 34 Illinois Law and Practice "Tenancy in Common" Sec. 13, commencing at page 313, that authority states:

"Each tenant in common of realty is equally entitled to the use, benefit, and possession of all the common property, and may exercise acts of ownership with respect thereto. (Cases cited) As stated by Justice Burke, speaking for the Appellate Court in *Massman*

v. *Duffy*, 1948 (333 Ill. App. 30) 'Subject to the rights of his co-tenants a co-tenant of real property may use and enjoy the common estate in the same manner as though he were the sole proprietor'."

(See also on this same point, 14 Am. Jur. "Co-tenancy," Sec. 24, Page 95, Note 10, and 86 C.J.S. "Tenancy in Common," Sec. 20, Page 379, note 52).

As a matter of law, the petitioner was a member of a joint adventure that included the respondent and the other members of the project. They pooled their funds and bought land for a site to build the motel, and also bought a parking lot and then constructed the motel.

As a member of this joint adventure and as a tenant in common the petitioner had the same absolute rights of control over the project that the other members had.

VIII.

JOINT ADVENTURES ARE NOT SUBJECT TO BLUE SKY STATUTES.

In *Brown* v. *Cole*, 155 Tex. 624, 291 S.W. 704 (1956), the court stated:

"[6] It is well settled that the Act does not apply to a joint adventurer and to transactions between joint adventurers. Joint adventurers and partners are not to be denied the right to recover their interest merely because of a failure to comply with the Securities Act and we think it equally true that a dissatisfied joint adventurer may not recover from other joint adventurers merely because of the failure of the latter to comply with the Act." *Polk* v. *Chandler*, 276 Mich. 527, 268 N.W. 732.

There was a similar holding in *Hathaway* v. *Porter Royalty Pool*, 295 N.W. 571, 299 N.W. 591, 138 A.L.R. 966.

53 C.J.S. "Licenses," Sec. 75, Page 764, Note 35, also states the rule that a joint adventure is not subject to Blue Sky Laws.

These State court decisions on State Blue Sky Laws are proper analogies to be considered in determining whether a particular transaction is covered by the Securities Act of 1933, as the general purposes of the State and Federal regulations are the same.

Sowards, Business Organizations — Securities Regulation—Federal Securities Act (Matthew Bender And Co. 1965) a recognized authority in this field has this to say in his recent work: (Section 2.01 (12), page 2-26)

"These factors, (attributes of a general partner) without more (and there are numerous others) seem to illustrate the marked difference between the ordinary *passive* investor in securities, who, under the Howey test, invests in a common enterprise 'with profits to come solely from the efforts of others', and the general partner, an active participant who expects to derive profits through *his* efforts.

This description of the general partner applies equally to the true joint venture; the joint venture has been defined as a partnership for a particular purpose. In short, a true general partnership (or joint venture) agreement is not a security." (Emphasis added by author)

IX.

JOINT ADVENTURE BETWEEN PARTIES CONTINUED NOTWITHSTANDING LATER FORMATION OF A CORPORATION, AND SUBSTITUTION OF NEW MEMBERS.

On February 3, 1962, *two years, two months and four days* after the petitioner made his first payment of $25,000.00 into the project, the respondents, it is alleged in

the petitioner's amended complaint, "caused a corporation to be organized and caused said real estate and motel to be transferred and conveyed to said corporation." (Abst. 14)

The petitioner refused to accept stock in the corporation so his original rights as a member of the joint adventure have not been prejudiced.

It is obvious that the corporation was formed as convenience for the project.

Hathaway v. *Porter Royalty Pool,* 296 Mich. 90, 733, 295 N.W. 571, 299 N.W. 451 (1941), 138 A.L.R. at Page 966, contains the following significant holding:

> "It is our conclusion that the agreement in question was an agreement for a joint adventure; that the formation of the corporation pursuant to the agreement in no way changed the relationship of joint adventure between the parties; that the agreement for the use of the corporate medium was only a convenient method of carrying into effect the joint adventure, and was not a contract within the prohibition of the blue sky law; that the issuance of stock by the corporation to the pool members was not the sale of securities, within the intendment of the statute."

Since the petitioner refused to accept the stock in the corporation that was formed, he still has all his original rights under the joint venture which is not subject to the Federal Securities Act.

The petitioner complains in his petition that there were changes in membership of the group. Some old members of the group dropped and new members were added. He made no objection to this.

During this period of more than two and one-half years, the substitution of new members did not terminate the joint adventure. (30 Am. Jur. "Joint Adventures," Sec. 32, Pages 960, 961, Note 15).

If, after new members are substituted the other members go forward upon the basis of the continuance of the adventure, there is no termination of the venture. (30 Am. Jur. "Joint Adventures," Sec. 32, Page 961, Note 18, citing *Meinhard* v. *Salmon*, 249 N.Y. 458, 164 N.E. 545, 62 A.L.R. 1)

The formation of a corporation and substitution of new members in the group did not impair the continued existence of the joint adventure of which the petitioner and the respondents were members.

X.

PETITIONER'S COMMENTS AS TO "REAL ESTATE SYNDICATION" INAPPLICABLE.

The State House Motor Hotel was not a "Syndicate." At Page 14 of the petitioner's petition he referred to "Kroll, The Why and How of Real Estate Syndications, Regulation Aspects, 5 The Practical Lawyer 70, 71 (March 1959)." At Page 71 of this article, we find the *Howey* test, after a discussion of "Investment Contract." Here is what Mr. Kroll stated at this point:

> "The courts and administrative agencies have put a substantial gloss on these catch-all phrases. They have come to include any arrangement whereby a person invests his money in a common enterprise with the expectation of deriving profits from the efforts of a promoter or some third party."

Also at Page 14 of the petitioner's petition he cited "Wein, The Why and How of Real Estate Syndications, How the Syndicate Functions, 5 The Practical Lawyer 54, 56 (March, 1959)." He made it clear in his article that a

real estate syndicate is a project where the investors pool their funds, purchase real estate, rent the property, and sit back and wait for profits from the rentals. If they cannot rent it, they have someone manage the property for them.

The petitioner and the other members of this motel joint venture did not lease it to third persons. They operated it themselves.

At Page 12 of the Petitioner's petition, he quoted from an article in 69 Yale Law Journal 725, at 764, note 166 (1960) on the topic of "Real Estate Syndication." That article made it clear that the purchasers in a real estate syndicate depend upon the integrity, judgment and ability of a syndicate manager for their investment rewards (p. 727).

Here are additional excerpts from that article:

> "With few exceptions, the syndicate investor does not participate actively either in the management of the property or in the decisions made by the syndicate entity. (p. 741) . . . not only is the syndicate investor a nonparticipant in the property management, but he may have little or no voice in the decision making processes of the syndicate entity. (p. 742) . . . An investment contract according to *Howey*, is a 'scheme' whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or third party. (p. 762) . . . The opinion stressed the investors' complete dependence upon their promoter's managerial efforts for their rewards, if any, and the resulting lack of control over the enterprise's expectancies . . . In evolving the concept of an investment contract as a security, therefore, the courts have emphasized the investors' dependence upon the promoter or a third party for profit. The SEC has welcomed this interpretation and has embellished it by formulating a pattern of practices tending to demonstrate promoter rather than investor control over the enterprise." (p. 763)

It is interesting to see that under footnote 163 at Page 763 there is this striking observation:

> "*S. E. C.* v. *W. J. Howey Co.*, 328 U.S. 293, 298 (1946), where the Supreme Court relied on state 'Blue Sky' decisions to determine the meaning of 'investment contract' in the Securities Act."

All of these excerpts from these articles can be summarized into the *Howey* test. Under the *Howey* test the joint adventure between the parties in the instant case was not subject to the Federal Securities Act of 1933.

XI.

RULES OF SECURITIES AND EXCHANGE COMMISSION INAPPLICABLE.

At Page 11 of the petitioner's petition there is a reference to Form S-11 of the Commission, and also to a notice that the Commission is considering a proposed form of registration. Both of these refer to *securities* to be issued by real estate syndicates, etc.

In the instant case we are not concerned with *securities* issued by a joint adventure.

Moreover, they are dated respectively April 10, 1961 and December 1, 1961, after the transactions in question occurred and could not have any *ex post facto* or retroactive effect.

On the same Page 11 of the petitioner's petition there is also a reference to Rule 3 A 11-1, adopted on April 23, 1965, by the Securities and Exchange Commission, wherein it is stated in the petition that the Commission defined "Equity security as including any . . . interest in a joint venture."

To begin with, this rule adopted on April 23, 1965 certainly also could not have any *ex post facto* or retroactive effect as to transactions that occurred in 1959 and 1960.

Petitioner's petition at page 11 admits that this Rule 3a 11-1, adopted on April 23, 1965, by the Securities and Exchange Commission was under the 1934 (not the 1933) Act.

Briefly, the 1933 Act relates to the registration requirements of Securities when they are issued. The 1934 Act relates to regulating the trading of securities after they are first issued.

In the instant case, the interest of the petitioner in the enterprise was not a "security" in any sense or under any statute. The petitioner was not an investor. He was a co-owner of real estate, a motor motel, and he had an equal right of management and control which he actively exercised.

The Securities and Exchange Commission issued its release No. 7581, dated April 23, 1965 with reference to the adoption of Rule 3a 11-1 and 12 h-2 under the Securities Exchange Act of 1934. (Rule 12 h-2 refers to exemptions that are not in issue in this case.)

In this release it is clear that this rule 3a 11-1 was adopted to define the term "equity security" as used in Section 12 g and Section 16 of the Amendments to the 1934 Act. (Securities Act of 1934, 15 U.S.C.A. 1934 Amendments to Sections 78 l and 78 p.)

The release went on to say:

> "Section 12 (g) of the act requires certain issuers with total assets exceeding $1,000,000 to file a registration statement with this Commission registering each class of its non-exempt equity securities which is held

of record by 750 or more persons at a fiscal year end after July 1, 1964, and each such class of equity securities held of record by 500 or more persons at a fiscal year end after July 1, 1966."

Section 16 of the Act refers to certain practices in trading in securities that are not pertinent to the instant case.

This Rule 3a 11-1 has no bearing in the case at bar.

There is nothing in any of these rules cited by the petitioner that conflicts with or modifies in any way the basic test in the *Howey* case.

None of these rules are applicable to the instant case.

CONCLUSION.

The petitioner has raised no conflict of decisions or any important question of Federal law which requires examination or decision by this court. The petitioner's petition is without merit in fact and in law, and should be denied.

Respectfully submitted,

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REPLY BRIEF OF PETITIONER IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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This Reply Brief is confined to pointing out the lack of merit in respondents' contention that this action under the Securities Act is barred by a statute of limitations, since that contention was not advanced below and has been injected into this case for the first time by respondents' Brief in Opposition (pp. 3-4).

Respondents assert that the suit, which was filed on November 7, 1962, was brought "more than a year after the last use of the mails" in the transaction (Brief in Opposition, p. 4). However, paragraph 11 of Count IV of the amended complaint alleges that "about February 3, 1962" respondents offered corporate stock to petitioner (Appendix to Petition, p. 17a), and paragraph 13 alleges that respondents "made use of the mails" in this connection (*id.*, at p. 18a). The amended complaint thus makes it clear

that this action, which is based on the unregistered offer to petitioner of units of investment, evidenced initially by "tentative receipts" and ultimately by shares of corporate stock, was brought within one year of respondents' last use of the mails in connection with the offer. Thus, even assuming *arguendo* respondents' view that the time of the last use of the mails determines the commencement of the limitations period, respondents' contention that limitations bars the action is without merit.

Respectfully submitted,

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